

TEST YOURSELF ON THE ACCOUNTING CYCLE

True or False

For each of the following statements, circle the T or the F to indicate whether the statement is true or false.

- T F 1. Publicly owned corporations have a legal obligation to release annual and quarterly financial information to their stockholders and to the public.
- T F 2. The statement of retained earnings must be prepared prior to preparing the income statement.
- T F 3. Net income reported in the income statement is an estimated figure, not an exact figure.

**Supplemental Topic, "The Worksheet."*

- | | | | |
|---|----|-----|---|
| T | F | 4. | Retained earnings reported in the balance sheet represents cash available for dividend distribution to stockholders. |
| T | F | 5. | Dividend expense is often the largest expense reported in a company's income statement. |
| T | F | 6. | The principle of adequate disclosure is more important to those who <i>prepare</i> financial statements than to those who <i>use</i> financial statements. |
| T | F | 7. | There is no comprehensive list of information that should be disclosed as notes to the financial statements. |
| T | F | 8. | Revenue, expenses, and dividends are referred to as nominal accounts. |
| T | F | 9. | The Dividends account is closed at the end of the period to the Income Summary account. |
| T | F | 10. | It is common practice for companies to make adjusting and closing entries on an annual basis. |
| T | F | 11. | If a company has been profitable, its Income Summary account will have a debit balance after all revenue and expense accounts have been closed to it. |
| T | F | 12. | An after-closing trial balance contains both income statement and balance sheet accounts. |
| T | F | 13. | The dollar amounts appearing in financial statements can be taken directly from an adjusted trial balance prepared at year end. |
| T | F | 14. | The dollar amounts appearing in financial statements cannot be determined until closing entries have been posted. |
| T | F | 15. | Financial statements normally are accompanied by several pages of "notes" supplying additional information. |
| T | F | 16. | A company that adjusts its books monthly and closes its books annually may prepare and close its books annually and may prepare quarterly financial statements directly from its adjusted trial balance at the end of each quarter. |
| T | F | 17. | A company need not close its books in order to prepare financial statements. |
| T | F* | 18. | A worksheet illustrates the relationship between an unadjusted trial balance, adjusting entries, and the amounts appearing in financial statements. |
| T | F* | 19. | Preparing a worksheet is a basic step in the accounting cycle. |
| T | F* | 20. | Worksheets are prepared only in manual accounting systems. |

*Supplemental Topic, "The Worksheet."

Completion Statements

Fill in the necessary word to complete the following statements:

1. When preparing a set of financial statements, the _____ is always prepared first.
2. In the statement of retained earnings _____ is added to the beginning retained earnings balance, whereas _____ are subtracted.
3. To the users of financial statements _____ is perhaps the most important accounting principle.
4. Most disclosures appear within the several pages of _____ that accompany the financial statements.
5. The journal entries made at the end of the accounting period to create zero balances in the temporary accounts are called _____ entries.
6. _____ and _____ accounts are closed at the end of the year by transferring their balances to the _____ account.
7. If a company has suffered a net loss for the period, its Income Summary account will have a _____ balance prior to being closed to the _____ account.
8. Unlike revenue and expense accounts, the _____ account is closed directly to the Retained Earnings account.
9. An _____ - _____ trial balance shows only _____ accounts.
- 10.* In the worksheet prepared by a business operating at a loss, the Income Statement _____ column will exceed the _____ column and the excess of the _____ over the _____ will be entered in the _____ column in order to bring the two Income Statement columns into balance.

*Supplemental Topic, "The Worksheet."

Multiple Choice

Choose the best answer for each of the following questions and enter the identifying letter in the space provided.

- ___ 1. Which of the following financial statements is prepared *first*?
 - a. Income statement.
 - b. Balance sheet.
 - c. Statement of retained earnings.
 - d. Statement of cash flows.

- ___ 2. Which of the following is *not* reported in a company's financial statements?
 - a. Advertising expense.
 - b. Depreciation expense.
 - c. Accumulated depreciation.
 - d. Highly skilled employees.

- ___ 3. Which of the following statements is correct?
 - a. Beginning retained earnings + net income – dividends = ending retained earnings.
 - b. Beginning retained earnings – net income + dividends = ending retained earnings.
 - c. Beginning retained earnings + net income + dividends = ending retained earnings.
 - d. Beginning retained earnings – net income – dividends = ending retained earnings.

- ___ 4. The declaration and payment of a cash dividend is reported in the:
 - a. Income statement as an expense.
 - b. Statement of cash flows as a source of cash.
 - c. Statement of retained earnings as a subtraction from beginning retained earnings.
 - d. None of the above.

- ___ 5. Which of the following is perhaps most important to *users* of financial statements?
 - a. Historical cost.
 - b. Objectivity.
 - c. Materiality.
 - d. Adequate disclosure.

- ___ 6. Which of the following accounts is *not* closed at the end of the year?
 - a. Dividends.
 - b. Accumulated Depreciation.
 - c. Depreciation Expense.
 - d. Income Summary.

- 7. Which of the following best describes a closing entry made by an *unprofitable* company?
- a. Debit Retained Earnings, credit Dividends.
 - b. Debit Income Summary, credit Retained Earnings.
 - c. Debit Retained Earnings, credit Income Summary.
 - d. Debit Dividends, credit Retained Earnings.
- 8. Which of the following accounts is *not* shown in an after-closing trial balance?
- a. Accumulated Depreciation.
 - b. Unearned Revenue.
 - c. Retained Earnings.
 - d. Dividends.
- 9. A business that prepares quarterly financial statements:
- a. Must close its accounts quarterly.
 - b. Must adjust its accounts at least quarterly.
 - c. May not issue annual financial statements.
 - d. Must obtain special permission from the IRS.
- 10.* The preparation of a *worksheet*:
- a. Constitutes creation of a formal financial statement.
 - b. Eliminates the need for entering adjusting entries in the journal.
 - c. Provides the information needed for journalizing adjusting and closing entries.
 - d. Serves no purpose unless the books are to be closed.
- 11.* When a worksheet is used, the normal sequence of accounting procedures would call for:
- a. Journalizing the adjusting entries before preparing the worksheet.
 - b. Posting adjusting entries to the ledger after preparing an after-closing trial balance.
 - c. Preparing a worksheet before journalizing adjusting and closing entries.
 - d. Journalizing closing entries before preparing an adjusted trial balance.
- 12.* Which of the following amounts appears in both the Income Statement credit column and the Balance Sheet debit column of a worksheet?
- a. Net income.
 - b. Net loss.
 - c. Accumulated depreciation.
 - d. Dividends.

*Supplemental Topic, "The Worksheet."

Exercises

1. Listed below are eight technical accounting terms emphasized in this chapter.

Adequate disclosure
Income summary
Interim financial statements
Current assets
Current liabilities

Closing entries
After-closing trial balance
Notes (accompanying financial statements)

Each of the following statements may (or may not) describe one of these technical terms. In the space provided below each statement, indicate the accounting term described, or answer "None" if the statement does not correctly describe any of the terms.

- a. Name given to monthly or quarterly income statements and balance sheets.

- b. Supplemental disclosures that aid financial statement users.

- c. A temporary account used to close revenue and expense items at year-end.

- d. The schedule from which a complete set of financial statements is prepared.

- e. The generally accepted accounting principle of including with financial statements a variety of information necessary to interpret the statements properly.

- f. The process at the end of the period by which the balances of temporary accounts are transferred to Retained Earnings.

- g. Resources that can be converted into cash or be used up within a relatively short period of time.

- h. Obligations expected to be satisfied within a relatively short period of time.

2. Using the adjusted trial balance shown below, prepare (a) an income statement, (b) a statement of retained earnings, and (c) a balance sheet for Fred's Pro Shop. Assume the business closes its accounts once each year on December 31.

Fred's Pro Shop
Adjusted Trial Balance
For the Year Ended December 31, 20__

	Debit	Credit
Cash	\$ 16,000	
Accounts receivable	39,000	
Supplies	3,000	
Shop equipment	25,000	
Accumulated depreciation: shop equipment		\$ 12,000
Accounts payable		6,000
Capital stock		30,000
Retained earnings		8,000
Dividends	1,000	
Fees earned		96,000
Rent expense	7,000	
Wages expense	44,000	
Supplies expense	2,000	
Depreciation expense: shop equipment	5,000	
Income taxes expense	10,000	
	<u>\$152,000</u>	<u>\$152,000</u>

a.

Fred's Pro Shop
Income Statement
For the Year Ended December 31, 20__

b.

**Fred's Pro Shop
Statement of Retained Earnings
For the Year Ended December 31, 20__**

c.

**Fred's Pro Shop
Balance Sheet
December 31, 20__**

- 3.* Use the following adjustments to complete the worksheet on the following page for the month ended January 31, 20__ (ignore income taxes).
- Unexpired insurance at January 31 amounted to \$300.
 - Office supplies on hand were determined by count to amount to \$250.
 - The office equipment is being depreciated on the basis of a 10-year life with no salvage value. Record one month's depreciation.
 - Accrued interest on notes payable at January 31 amounted to \$50.
 - Commissions still unearned at January 31 amounted to \$700.
 - Accrued salaries payable at January 31 were \$2,100.

SOLANA CORPORATION
Worksheet
For the Month Ended January 31, 20__

	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Balance Sheet	
	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit
Balance sheet accounts:										
Cash	12,960									
Accounts receivable	17,300									
Unexpired insurance	360									
Office supplies	900									
Office equipment	25,200									
Accumulated depreciation:										
office equipment		3,150								
Notes payable		10,000								
Accounts payable		1,800								
Unearned commissions		1,500								
Capital Stock		20,000								
Retained Earnings		12,000								
Interest payable										
Salaries payable										
Income statement accounts:										
Commissions earned		21,670								
Rent expense	2,400									
Salaries expense	11,000									
	70,120	70,120								
Insurance expense										
Office supplies expense										
Depreciation expense: office eqpt										
Interest expense										
Net income										

*Supplemental Topic, "The Worksheet."

4.* On the journal page following, prepare adjusting and closing entries using the information contained in the worksheet prepared in Exercise 3.

[illegible]

**Supplemental Topic, "The Worksheet."*